

# ORIGINAL EXCEPTION

OPEN MEETING AGENDA ITEM

BEFORE THE ARIZONA CORPORATION

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## COMMISSIONERS

2004 MAY 17 P 3:09

MARC SPITZER - Chairman  
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AZ CORP COMMISSION  
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Arizona Corporation Commission

DOCKETED

MAY 17 2004

DOCKETED BY

IN THE MATTER OF THE APPLICATION OF  
ARIZONA-AMERICAN WATER COMPANY, INC.,  
AN ARIZONA CORPORATION, FOR A  
DETERMINATION OF THE CURRENT FAIR  
VALUE OF ITS UTILITY PLANT AND  
PROPERTY AND FOR INCREASES IN ITS RATES  
AND CHARGES BASED THEREON FOR UTILITY  
SERVICE BY ITS SUN CITY WEST WATER AND  
WASTEWATER DISTRICTS.

DOCKET NO. WS-01303A-02-0867

IN THE MATTER OF THE APPLICATION OF  
ARIZONA-AMERICAN WATER COMPANY, INC.,  
AN ARIZONA CORPORATION, FOR A  
DETERMINATION OF THE CURRENT FAIR  
VALUE OF ITS UTILITY PLANT AND  
PROPERTY AND FOR INCREASES IN ITS RATES  
AND CHARGES BASED THEREON FOR UTILITY  
SERVICE BY ITS SUN CITY WATER AND  
WASTEWATER DISTRICTS.

DOCKET NO. WS-01303A-02-0868

IN THE MATTER OF THE APPLICATION OF  
ARIZONA-AMERICAN WATER COMPANY, INC.,  
AN ARIZONA CORPORATION, FOR A  
DETERMINATION OF THE CURRENT FAIR  
VALUE OF ITS UTILITY PLANT AND  
PROPERTY AND FOR INCREASES IN ITS RATES  
AND CHARGES BASED THEREON FOR UTILITY  
SERVICE BY ITS MOHAVE WATER DISTRICT  
AND ITS HAVASU WATER DISTRICT.

DOCKET NO. W-01303A-02-0869

IN THE MATTER OF THE APPLICATION OF  
ARIZONA-AMERICAN WATER COMPANY, INC.,  
AN ARIZONA CORPORATION, FOR A  
DETERMINATION OF THE CURRENT FAIR  
VALUE OF ITS UTILITY PLANT AND  
PROPERTY AND FOR INCREASES IN ITS RATES  
AND CHARGES BASED THEREON FOR UTILITY  
SERVICE BY ITS MOHAVE WATER DISTRICT  
AND ITS ANTHEM WATER DISTRICT, ITS  
AGUA FRIA WATER DISTRICT, AND ITS  
ANTHEM/AGUA FRIA WASTEWATER  
DISTRICT.

DOCKET NO. WS-01303A-02-0870

STAFF'S EXCEPTIONS TO  
RECOMMENDED  
OPINION AND ORDER

1 IN THE MATTER OF THE APPLICATION OF  
2 ARIZONA-AMERICAN WATER COMPANY, INC.,  
3 AN ARIZONA CORPORATION, FOR A  
4 DETERMINATION OF THE CURRENT FAIR  
5 VALUE OF ITS UTILITY PLANT AND  
6 PROPERTY AND FOR INCREASES IN ITS RATES  
7 AND CHARGES BASED THEREON FOR UTILITY  
8 SERVICE BY ITS TUBAC WATER DISTRICT.

DOCKET NO. W-01303A-02-0908

**STAFF'S EXCEPTIONS TO  
RECOMMENDED  
OPINION AND ORDER**

6 Staff does not take exception to any of the language in the Recommended Opinion and Order  
7 ("ROO"). Indeed, Staff concurs in the thoughtful analysis contained in the ROO. However, Staff  
8 notes that the numbers in the ROO and schedules to the ROO appear to be inconsistent with the text  
9 of the ROO. It appears that three important miscalculations occurred.

10 First, the calculation of (1) overheads; (2) salaries and wages; and (3) service company  
11 charges is incorrect. It appears that the ROO used Arizona-American's rejoinder schedules as a  
12 starting point. Following the text of the ROO, Arizona-American's calculation of the three items  
13 listed above should have been replaced by RUCO's figures for these items. However, instead of  
14 removing Arizona-American's amounts and recognizing RUCO's amounts, it appears that the reverse  
15 occurred. That is, an amount equal to RUCO's adjustments was removed, and an amount equal to  
16 Arizona-American's amounts was added. This appears to be a simple calculation error.

17 Second, it appears that the ROO numbers used the property tax expense from Arizona-  
18 American's rejoinder schedules instead of an amount consistent with the text that adopts Staff's  
19 method for calculating property tax expense.

20 Third, the calculation of income tax is incorrect. Staff was not able to determine all of the  
21 reasons for this miscalculation. In part, the error was due to using an incorrect level of interest  
22 expense to calculate the income tax. It appears that synchronized interest was not used for the  
23 interest expense in the income tax calculation. Income tax expense is also affected by the  
24 aforementioned operating expense treatments.

25 ...

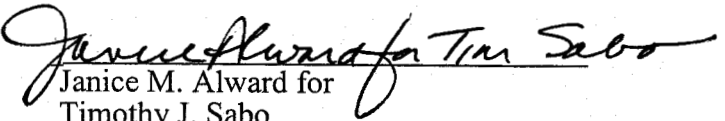
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1 Staff corrected the three errors discussed above. These corrections are shown on the attached  
2 Exhibit A. The total effect of these errors for each system is shown on Exhibit B. Staff respectfully  
3 requests that the Commission approve modifications to the ROO consistent with these attached  
4 schedules, and that rates be adjusted accordingly.

5 RESPECTFULLY SUBMITTED this 17th day of May 2004.

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8   
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13 The original and twenty-one (21) copies  
14 of the foregoing were filed this  
15 17<sup>th</sup> day of May 2004 with:

15 Docket Control  
16 Arizona Corporation Commission  
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18 Phoenix, Arizona 85007

18 Copies of the foregoing were mailed  
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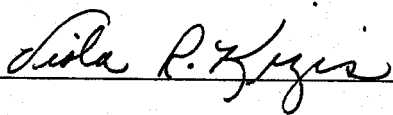
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REVENUE REQUIREMENT INCREASE/(DECREASE) - BY SYSTEM  
(STAFF EXCEPTIONS)

Line No.	Description	Sun City West Water	Sun City West Wastewater	Sun City Water	Sun City Wastewater	Mohave Water	Havasu Water	Anthem Water	Aqua Fria Water	Anthem/Wastewater	Tubac Water
1	Test Year Revenue	\$ 3,380,774	\$ 3,535,680	\$ 6,193,090	\$ 5,088,340	\$ 4,394,132	\$ 440,924	\$ 4,010,805	\$ 6,186,037	\$ 1,866,546	\$ 254,466
2	Test Year Operating Expenses	2,938,753	3,895,951	6,030,993	4,091,048	3,404,484	396,767	3,023,829	4,550,576	1,830,365	245,434
3	Test Year Operating Income	442,021	(360,271)	162,097	997,292	989,648	44,157	986,976	1,635,461	36,181	9,052
4	Required Operating Income	777,652	579,195	1,421,483	566,207	571,239	53,442	1,083,417	602,858	177,535	73,271
5	Operating Income Deficiency/(Excess)	335,631	939,466	1,259,386	(431,085)	(418,409)	9,285	96,441	(1,032,603)	141,354	64,219
6	Gross Revenue Conversion Factor	1.62863	1.62863	1.62863	1.62863	1.62863	1.62863	1.62863	1.62863	1.62863	1.62863
7	Increase in Gross Revenue Requirement	\$ 546,619	\$ 1,530,042	\$ 2,051,073	\$ (702,077)	\$ (681,433)	\$ 15,121	\$ 157,066	\$ (1,681,728)	\$ 230,213	\$ 104,588
8	Required Percent Increase/(Decrease) in Revenue	16.17%	43.27%	33.12%	-13.80%	-15.51%	3.43%	3.92%	-27.19%	12.33%	41.10%

Calculation of Test Year Operating Expenses

9	Total Operating Expenses - Company Rejoinder	\$ 2,932,836	\$ 3,578,308	\$ 5,611,752	\$ 3,958,033	\$ 3,478,133	\$ 428,168	\$ 3,279,318	\$ 4,845,829	\$ 1,848,102	\$ 236,000
10	Additions:										
11	Rate Case Expense	13,355	13,966	24,464	20,100	17,368	1,742	15,839	24,436	7,373	1,006
12	OVHD - Salaries and Wages	22,464	33,696	89,857	14,976	56,161	11,232	44,928	26,208	22,464	3,744
13	OVHD - Office Supplies	182,392	168,783	322,580	242,477	163,185	14,208	53,684	165,421	30,213	9,386
14	OVHD - Insurance	19,535	16,021	57,988	24,091	18,113	1,630	11,712	22,645	3,398	2,351
15	OVHD - Miscellaneous	1,464	1,238	4,408	1,686	1,848	1,297	5,332	6,263	5,176	277
16	Salaries and Wages	270,185	740,226	906,640	354,605	671,552	68,018	274,925	371,660	166,340	65,086
17	Service Company Charges	437,097	468,101	784,680	442,774	441,464	63,753	399,982	604,339	277,965	32,750
18	Property Tax	144,412	162,599	240,067	177,169	240,404	25,489	112,294	280,269	107,303	21,046
19	Subtotal Operating Expense Additions	1,090,904	1,604,630	2,430,684	1,277,878	1,610,033	187,369	918,696	1,501,241	620,232	135,646
20	Federal and State Income Taxes	60,452	(231,346)	(15,974)	219,526	253,706	20,964	273,347	406,090	(2,201)	(2,209)
21	Total Additions	\$ 1,151,356	\$ 1,373,284	\$ 2,414,710	\$ 1,497,404	\$ 1,863,799	\$ 208,333	\$ 1,192,043	\$ 1,907,331	\$ 618,031	\$ 133,437
22	Deletions:										
23	Rate Case Expense	22,313	23,335	40,874	33,583	29,013	2,910	26,471	43,906	12,319	1,680
24	OVHD - Salaries and Wages	57,666	86,499	230,664	38,444	144,165	28,833	115,332	115,332	57,666	9,611
25	OVHD - Office Supplies	104,573	92,664	214,090	131,056	92,327	9,420	45,501	108,264	23,372	7,080
26	OVHD - Insurance	22,010	17,430	63,152	24,520	19,040	1,736	13,731	26,166	3,979	2,471
27	OVHD - Miscellaneous	1,462	1,237	4,389	1,685	1,840	1,288	5,300	6,226	5,142	275
28	Salaries and Wages	332,908	413,655	769,786	69,343	576,845	110,136	302,138	430,190	199,310	64,491
29	Service Company Charges	474,642	508,522	852,438	481,009	479,586	69,258	434,521	656,525	264,697	35,578
30	Property Tax - Company Rejoinder	130,976	163,121	266,318	186,357	263,528	27,185	221,191	309,791	108,825	22,972
31	Federal and State Income Taxes - Company Rejoinder	(1,311)	(250,822)	(446,242)	395,392	331,104	(13,032)	283,347	506,184	(39,542)	(20,135)
32	Total Operating Expense Deletions	1,145,439	1,055,641	1,995,469	1,364,389	1,937,448	237,734	1,447,532	2,202,584	635,768	124,003
33	Total Test Year Operating Expenses	\$ 2,838,753	\$ 3,895,951	\$ 6,030,993	\$ 4,091,048	\$ 3,404,484	\$ 396,767	\$ 3,023,829	\$ 4,550,576	\$ 1,830,365	\$ 245,434

Calculation of Test Year Income Taxes

34	Test Year Revenue	\$ 3,380,774	\$ 3,535,680	\$ 6,193,090	\$ 5,088,340	\$ 4,394,132	\$ 440,924	\$ 4,010,805	\$ 6,186,037	\$ 1,866,546	\$ 254,466
35	Less: Total Operating Expenses - Company Rejoinder	2,932,836	3,578,308	5,611,752	3,958,033	3,478,133	426,168	3,279,318	4,845,829	1,848,102	236,000
36	Less: Subtotal Operating Expense Additions	1,090,904	1,604,630	2,430,684	1,277,878	1,610,033	187,369	918,696	1,501,241	620,232	135,646
37	Add: Total Operating Expense Deletions Except Income Tax	1,145,750	1,306,463	2,441,711	968,997	1,606,344	250,766	1,184,185	1,896,400	675,310	144,138
38	Synchronized Interest Expense	347,167	258,564	633,751	292,688	234,960	23,841	288,804	483,290	79,224	32,702
39	Taxable Income - Test Year	155,617	(598,359)	(41,386)	568,738	657,290	54,312	708,172	1,052,077	(5,702)	(5,724)
40	State Tax @ 6.988%	10,913	(41,763)	(2,884)	39,630	45,800	3,784	49,345	73,309	(397)	(399)
41	Federal Taxable Income	145,704	(557,596)	(38,502)	529,108	611,490	50,527	658,827	978,768	(5,305)	(5,325)
42	Federal Tax @ 34%	49,539	(189,583)	(13,091)	179,897	207,906	17,179	224,001	332,781	(1,804)	(1,811)
43	Total Federal & State Income Taxes	\$ 60,452	\$ (231,346)	\$ (15,974)	\$ 219,526	\$ 253,706	\$ 20,964	\$ 273,347	\$ 406,090	\$ (2,201)	\$ (2,209)

Calculation of Synchronized Interest

44	Original Cost Rate Base	\$ 11,971,281	\$ 8,916,017	\$ 21,853,479	\$ 8,713,382	\$ 8,791,741	\$ 822,117	\$ 9,289,095	\$ 16,665,182	\$ 2,731,868	\$ 1,127,661
45	Weighted Average Cost of Debt	2.90%	2.90%	2.90%	2.90%	2.90%	2.90%	2.90%	2.90%	2.90%	2.90%
46	Synchronized Interest Expense	\$ 347,167	\$ 258,564	\$ 633,751	\$ 252,688	\$ 254,960	\$ 23,841	\$ 288,804	\$ 483,290	\$ 79,224	\$ 32,702

Calculation of Test Year Income Tax Adjustment

44	Total Federal & State Income Taxes	\$ 60,452	\$ (231,346)	\$ (15,974)	\$ 219,526	\$ 253,706	\$ 20,964	\$ 273,347	\$ 406,090	\$ (2,201)	\$ (2,209)
45	Federal and State Income Taxes - Company Rejoinder	(1,311)	(250,822)	(446,242)	395,392	331,104	(13,032)	278,403	506,184	(39,542)	(20,135)
46	Test Year Income Tax Adjustment	\$ 61,763	\$ 19,476	\$ (430,268)	\$ (598,565)	\$ (77,398)	\$ 33,996	\$ (5,056)	\$ (100,094)	\$ 37,341	\$ 17,926

REVENUE REQUIREMENT BY SYSTEM - ROO vs REVISED  
(STAFF EXCEPTIONS)

Line No.	Description	Sun City West Water	Sun City West Wastewater	Sun City Water	Sun City Wastewater	Mohave Water	Havasu Water	Anthem Water	Aqua Fria Water	Anthem/ Aqua Fria Wastewater	Tubac Water
1	Increase/(Decrease) in Gross Revenue - ROO	\$ 604,642	\$ 1,143,789	\$ 1,639,864	\$ (1,370,862)	\$ (385,925)	\$ 87,067	\$ (132,865)	\$ (539,990)	\$ 229,038	\$ 70,145
2	Increase/(Decrease) in Gross Revenue - Revised	\$ 546,619	\$ 1,530,042	\$ 2,051,073	\$ (702,077)	\$ (681,433)	\$ 15,121	\$ 157,066	\$ (1,681,728)	\$ 230,213	\$ 104,588
3	Increase/(Decrease) to ROO Revenue Requirement L2-L1	\$ (58,023)	\$ 386,253	\$ 411,209	\$ 668,785	\$ (295,508)	\$ (71,946)	\$ 289,931	\$ (1,141,738)	\$ 1,175	\$ 34,443
4	Revenue Requirement - ROO	\$ 3,985,416	\$ 4,679,469	\$ 7,832,954	\$ 3,717,478	\$ 4,008,207	\$ 527,991	\$ 3,877,940	\$ 5,646,047	\$ 2,095,584	\$ 324,631
5	Revenue Requirement - Revised	\$ 3,927,393	\$ 5,065,722	\$ 8,244,163	\$ 4,386,263	\$ 3,712,699	\$ 456,045	\$ 4,167,871	\$ 4,504,309	\$ 2,096,759	\$ 359,074